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NEW YORK STATE COMMISSION ON CABLE TELEVISION

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August 24, 1993

Donna R. Searcy, Secretary
Federal Communications Commission
1919 M Street, N.W.
Washington, DC 20554

Re: MM Docket No. 93-215

Dear Ms. Searcy:

I am enclosing herewith an original and nine copies of comments submitted by the New York State Commission on Cable Television in the above-referenced proceeding.

Very truly yours,

John L. Grow
Counsel

JLG:tac

Enclosures

NEW YORK STATE COMMISSION ON CABLE TELEVISION

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of

Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Docket No. 93-215
Rate Regulation	)	

COMMENTS OF THE NEW YORK STATE COMMISSION ON CABLE TELEVISION

1. The New York State Commission on Cable Television ("NYSCCT") respectfully submits initial comments in response to the Notice of Proposed Rulemaking ("NPRM") released in this docket July 16, 1993. NYSCCT is an independent Commission with broad authority to promote and oversee the development of the cable television industry in the state of New York. NYSCCT is expressly authorized by Section 815(6) of the Executive Law of the State of New York to represent the interests of the people of the State before the Federal Communications Commission ("Commission").

2. Earlier this year, the Commission adopted a benchmark and price cap approach as the primary method for the regulation of cable rates. The reasons that entered into this determination are reviewed at paragraph 4 of the NPRM wherein the Commission states that it determined that the benchmark/price cap approach was preferred because of the "disadvantages associated with cost of service regulation, including increased

administrative burdens imposed on cable operators and regulators." This concern for the disadvantages of cost based rate-of-return regulation is reiterated in paragraph 12 in the context of a discussion of regulatory goals for this proceeding. The Commission states:

> "[d]etermination and evaluation of cost-based rates can be a complex and resources intensive activity. In-depth evaluation of cost-based rates for many cable operators would impose significant administrative burdens on cable operators and regulators. Therefore, we believe that our requirements for cost-based rates must, to the extent possible, be based on a pragmatic approach geared to the feasibility of implementation of cost-based regulation by local regulators and the Commission. We believe that to the extent possible, our regulations should be designed to reduce administrative burdens on cable operators and regulators."

Elsewhere, the Commission notes that when regulating other telecommunications industries it has sought to develop alternatives to traditional cost-based rate regulation (para. 16) and that "[c]urrently only a few rate-based rate-of-return proceedings are conducted each year by all authorities practicing cost-of-service regulation." (Para. 60)

3. It is precisely because of the complexity and burdens of cost-of-service regulation that NYSCCT urges the Commission to pursue with the utmost diligence various of the "streamlining alternatives" described in paragraphs 70-75 of the NPRM. The Commission suggests two general approaches that might permit the establishment of cost-based rates without full cost-of-service proceedings. The first general approach would be an alternative to the benchmark approach that would avoid cost-of-service proceedings altogether. The second general approach would be a reduced or abbreviated cost-of-service showing. With respect to each approach, the Commission suggests a number of possibilities.

Although we are unable at this time to endorse specific proposals for streamlining cost-based regulation, we heartily encourage the Commission to pursue alternatives. The Commission should endeavor to collect cost data from the cable industry towards the goal of identifying key financial characteristics or cost factors that might account for cable rate differentials in a significant percentage of cases and of developing alternatives based on such factors or characteristics. The Commission need not restrain itself to the formulation of a single alternative but should consider a variety of reasonable alternatives. As noted by the Commission in the context of discussing the relative merits of MSO-wide cost averaging, "it is conceivable that thousands of cost-of-service showings may be filed, with any single MSO a party to hundreds of such proceedings." (Para. 60) The prospect of even hundreds of full cost-of-service proceedings is alone sufficient reason to develop alternatives.

4. The special interest of NYSCCT in more efficient and less onerous methods for determining reasonable cost-based rates coincides with its concern about the impact of the new regulatory scheme on the many small cable operators and small municipalities in New York State and across the country. In paragraphs 76-78, the Commission solicits comments on various issues pertaining to small systems. For example, the Commission asks whether small systems should be exempt from all regulation. It is doubtful that the intent of Congress and the public interest can be best served by exempting small cable systems from rate regulation altogether. Subscribers to such systems should have some protection. On the other hand, the Commission should recognize that regulatory burdens would be minimized if small operators and their respective franchising authorities were free to establish rates by negotiation. This could serve the interests of the Commission

as well as the interests of small franchising authorities and small system operators. A small cable operator, for instance, could protect against the need to participate in a proceeding at the faraway Commission by collapsing all programming into the basic tier subject to agreement with the local franchising authority over the rates therefor. Another alternative means of easing the burden of regulation for small systems would be to permit small systems and their franchising authorities to choose to abide by any of the benchmark rates applicable to systems under 1,000. The six (of a total of eight) benchmark tables applicable to cable systems with fewer than 1,000 subscribers show that the meaningful differences exist mainly between the very small -- 50 and 100 subscriber systems. We suggest that a small cable operator and a franchising authority should be permitted to decide among the per-channel benchmark rates for systems under 1,000. Of course, the Commission should not preclude the opportunity for even a small operator to employ cost-of-service even though we can't imagine that any would choose to do so. We do believe that the Commission acted wisely in deferring the effective date of the new rate regulations as applied to small systems.

5. NYSCCT generally agrees with the other regulatory goals stated by the Commission in paragraphs 7-14 of the NPRM. In particular, we agree with the Commission's view that "cable operators can, and should, contribute to the continued development of an advanced telecommunications infrastructure" and with the Commission's tentative conclusion that "regulatory requirements for cost-based rates should. . .be designed to assure that cable operators may fully respond to incentives to provide a modern communications infrastructure and to respond to competitive forces." (Para. 16) NYSCCT endorses this regulatory goal. Moreover, in this regard, we note that in both the NPRM and

in the Report and Order adopting the benchmark/price cap method in Docket No. 93-266, the Commission has neglected to recognize explicitly that the construction obligations of the cable operator, including capacity and other facilities and equipment requirements, are a common feature of many cable television franchises and, as such, may properly be considered franchise costs. In New York State, for example, NYSCCT as well as various municipal governments have acted to approve the transfer or renewal of cable television franchises only upon condition that the franchisee undertake substantial upgrades or rebuilds of cable systems within a defined time frame. The Commission's cost-of-service standards should not unreasonably jeopardize the fulfillment of these franchise requirements. Capital expenditures to upgrade system capacity and service should be included in a cable operator's rate base.

6. Certain other issues could have a direct impact on the fulfillment by cable operators of franchise requirements for facilities and equipment. The Commission proposes to use the original cost method for valuation of cable televisoin systems. It appears that the Commission believes that operators can readily determine original cost from their accounts. It is the experience of NYSCCT that original costs are not easily determined because of the transfer of cable systems over time and the removal of records by prior owners. If, however, the Commission adopts rules requiring original cost valuation, NYSCCT agrees that "equity may require allowance of some excess acquisition costs in view of the transition from a nonregulated to a regulated environment." (Para. 39) The Commission tentatively concludes that it should exclude excess acquisition costs from rate base but provide cable operators with an opportunity to demonstrate the need for inclusion of some or all of such

costs as a transition mechanism. (Para. 40) The Commission also asks for comment on whether excess acquisition costs should be allowed as an annual expense and, if so, the appropriate period therefor. NYSCCT agrees that excess acquisition costs should be allowed as an annual expense amortized over a period, perhaps shorter than 40 years, and also agrees with the Commission that a cable operator should be permitted to demonstrate the need to include excess acquisition costs in the rate base itself. In this regard, while NYSCCT recognizes that prices paid for the acquisition of cable systems since deregulation in 1984, and particularly in the latter part of the 1980's, were substantially in excess of the cost of constructing a cable system, many such transfers were subject to government consents (and, as noted, to substantive requirements for system modernization) and the inflated prices were not unique to the cable television industry.

7. As a related matter, in paragraph 53 of the NPRM, the Commission addresses the issue of the appropriate cost for debt. The Commission tentatively concludes that the methodology for measuring the cost of debt will be largely a factual examination of the cost of debt of a surrogate industry. The Commission solicits comment on whether it should accord any weight to existing (embedded) debt of the cable industry in determining an appropriate cost of debt. It is the view of NYSCCT that some reasonable weight should be accorded to embedded debt in determining an appropriate cost of debt, at least during the transitional phase.

8. Treatment of construction work in progress is also an important issue relative to infrastructure development. The Commission asks whether it should apply the traditional rule that "plant under construction will be withheld from rate base until it meets

"the used and useful test, but that interest during construction can be capitalized." (Para. 42) The general rule may be appropriate in many cases; however, we believe that the rules should also permit regulating franchising authorities to examine whether construction costs, or a portion thereof, might properly be included in the rate base prior to completion.

9. The Commission also seeks comment on the appropriate treatment of excess capacity, cost overruns and premature abandonments, suggesting that it might exclude these costs from rate base or, alternatively, avoid regulatory limitations at this time and monitor industry practices for the imposition of requirements later, if necessary. (para. 43) We note, initially, that the concept of "excess capacity" as it applies to cable television systems may be difficult to apply. Where a franchise requires a cable operator to rebuild or upgrade a system to a specified minimum capacity, we do not believe that the concept of "excess capacity" is relevant. Given the capital intensive nature of plant construction for cable television systems and the emphasis of federal and state policy on diversity of programming, available, but temporarily unused, channel distribution capacity is decidedly in the public interest and should not be excluded from the rate base.

10. The Commission has asked for comments on a variety of issues relative to depreciation. (Paras. 25-29) NYSCCT does not oppose the prescription by the Commission of depreciation requirements provided that such requirements are based on a straight line method and include a band of industry-wide reasonable rates with a band of individual rates for each plant category. Surely, we think that depreciation should be uniform on a cable system-wide basis. With respect to salvage value, it is our view that salvage value for cable plant and equipment should be zero.

11. In paragraphs 17-20, the Commission also offers various proposals concerning the procedural requirements for cost-of-service showings. First, the Commission proposes to limit the frequency with which a cable operator may make a cost-of-service showing to one showing for each tier per year. The stated purpose of this proposal is to eliminate the burdens of repetitive filings. NYSCCT supports the concept of limiting cost-of-service showings. Although annual rate filings are the norm in regulated industries, they could impose substantial regulatory burdens on franchising authorities and the Commission alike. Accordingly, we urge the Commission to consider rules that would permit multi-year rate setting for a pre-determined rate period, e.g., up to three years, allowing for known changes in increments for taxes, contract or labor cost, inflation, etc.

12. Second, the Commission asks whether it should establish procedural limits or bars on cost-of-service showings "absent a demonstration of special circumstances or extraordinary costs." We oppose the imposition of special circumstances on use of cost-of-service showings in favor of further efforts by the Commission to develop either alternative standards for reasonable rates or abbreviated cost-of-service proceedings. (Supra, para. 3) Indeed, if a company chooses not to adjust its rates to benchmark levels it may be presumed that there are unusual or exceptional circumstances which the operator believes warrants a cost-of-service showing.

13. Third, the Commission proposes in paragraph 19 to require that cost-of-service showings and supporting data be presented on a form and associated work sheets prescribed by the Commission. In support of this proposal, the Commission states its belief that such a form would "generally reduce administrative burdens by providing for a uniform

presentation of development of cost-based rates for cable service." Such a form is fully consistent with form 393 and associated work sheets which are required by the Commission to be used by cable companies to demonstrate the reasonableness of rates in accordance with the benchmark method. Since the Cable Act of 1992 and Commission rules will permit coincidental proceedings at the Commission level relative to rates for cable programming services and at the franchising authority level for basic service rates, a single prescribed form will facilitate review and help to ensure consistency in the presentations made by cable operators.

14. Consistency is also particularly relevant to the issue of cost allocation requirements. Specifically, in reference to the Commission's discussion of cost averaging, NYSCCT agrees with the Commission that averaging would reduce duplicative regulatory investigations. (Para. 62) As a practical matter, we think that systemwide cost averaging is already the case in most instances and should be required by the Commission. We are not persuaded at this time that MSO-wide cost averaging is warranted even though it is clearly preferable to franchise specific data. In reference to the latter, an obligation to keep such information would be clearly burdensome and a departure from cable industry record-keeping in the past as we know it. In this regard, "[m]ost cable customers are served by franchises that are not stand-alone, discreet units either operationally or financially." (Para. 46, fn. 48) The need for consistency is manifest in the possibility for coincidental cost-of-service showings, as noted. (Supra, para. 13) It is essential that cost allocations made in such circumstances be based on the same underlying costs and cost allocation concepts.

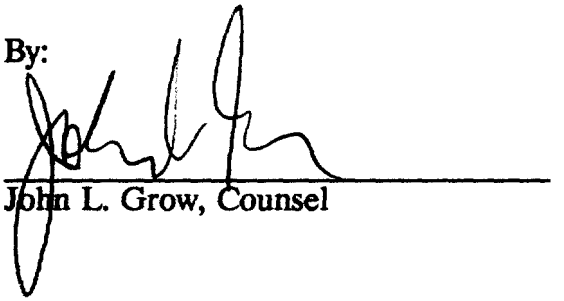
15. For the same reason that we support allocation on a system-wide basis, we agree with the Commission that it is not practical to have separate approved rates-of-return for each franchise area. (Para. 46) We agree with the Commission's observation, (also in footnote 48) that "it appears that there are no well accepted and readily calculable methods for isolating the business and financial risks associated with an individual franchised regulated cable service." Indeed, "[t]he difficulties inherent in identifying and valuing the financing supporting an individual franchise" are daunting. On the other hand, it is our view that the financial structures of cable companies are much too diverse to require a single, industry-wide rate-of-return standard. In this regard, we ask the Commission to consider dividing companies into two categories -- publicly traded companies and privately held companies. In addition, we are not opposed to the authorization or a range of rates-of-return for groups or types of systems.

16. In sum, we agree with the Commission that the cost-of-service requirements should form a "backstop" for the benchmark approach to rate regulation only. We suspect that as a rate-setting method it will be rarely used but the rules must be prepared for employment on a larger scale. Accordingly, we reiterate our encouragement to the Commission to collect additional data on the cost and financial characteristics, including capital structures, of the cable industry in order to develop alternative means for determining reasonable rates under the Cable Act of 1992. We might remind the Commission that cable rates were subject to regulation throughout most of the country prior to 1984 and in most cases the rates were set by negotiation between the cable operator and the franchising authority. As one considers the myriad of issues related to cost-of-service

it is ironic that the federal government is embarking on traditional cost-based regulation of cable at a time when it has abandoned the same for other regulated interests. It is even more unfortunate that in restoring regulation of cable television rates, the federal government has chosen a path that imposes almost as much regulation on state and local governmental discretion in this matter as it does on the cable industry itself.

Respectfully submitted,

NEW YORK STATE COMMISSION
ON CABLE TELEVISION

By: 

John L. Grow, Counsel

Dated: August 24, 1993
Albany, New York